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C O N F I D E N T I A L SECTION 01 OF 03 ISLAMABAD 000191

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E.O. 12958: DECL: 01/09/2013

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SUBJECT: AMBASSADOR PATTERSON MEETS WITH CARETAKER FINANCE MINISTER
SALMAN SHAH

Classified by CDA Peter W. Bodde for reasons 1.4(b) and (d)

¶1. SUMMARY. In a January 4 meeting with caretaker Minister of Finance Salman Shah, Ambassador Patterson inquired about the state of Pakistan's economy following the violence after Bhutto's December 27 assassination and raised commercial advocacy issues, coalition support funds, anti-money laundering legislation, and the \$200 million cash transfer (aka Shared Objectives). Ambassador suggested that Pakistan accept technical assistance from the USG with Department of Treasury experts coming to Pakistan for an exchange visit on establishing a financial monitoring unit. Shah noted that the GOP would welcome such an exchange as soon as possible. END SUMMARY.

¶2. (SBU) Ambassador met with Interim Finance Minister Salman Shah January 4 and delivered a non-paper on outstanding U.S. commercial advocacy issues which are pending before the Government of Pakistan (GOP)(Comment: Emailed to EEB and SCA).

Economic impact of post-Bhutto assassination violence

¶3. (C) In response to the Ambassador's concerns about the monetary loss after recent violence following Benazir Bhutto's December 27 assassination, Shah noted that the dollar impact is still being tabulated and will not be truly known for some time. Shah considered that the damage has three different aspects: Pakistan's reputation, production disruptions, and how the actual loss of life, property, and vital infrastructure which was targeted impacts the overall economy and future industrial production overall. The damage to Pakistan's reputation as a place to do business may well exceed the dollar costs.

¶4. (C) Ambassador asked if Shah is seeing a loss of confidence from outside investors. Shah noted that the GOP had been "managing the investment environment well" and the Karachi stock market was "behaving well overall," but there was a qualitative difference during the three days of violence. He maintained that security must be tighter and people must understand what enormous consequences are at stake for the country. He blamed the local and international media for exacerbating the problems. Shah noted that moving forward with the economic privatization and liberalization reforms will be critical to continue economic and investor-lead growth which Pakistan has enjoyed during Musharraf's term.

¶5. (C) Noting a "confluence of issues from American companies lately," Ambassador noted there was beginning to be nervousness about the state of the overall economy. The Ambassador raised several

commercial advocacy issues which are currently "causing confusion with the interim caretaker government." Notably, Chevron is owed USD 44 million in back payments to cover differentials in the international market and point of sale prices for gasoline and other fuels from July to December 2007. Oracle and Motorola have each recently been notified of additional specifications added to pending or previously awarded procurement tenders. Microsoft has an unanswered settlement offer to the GOP of USD ten million to settle its claims against the GOP for using pirated Microsoft software.

¶6. (C) While rightfully noting that the Ministry of Finance does not have a role in all of these issues, Shah acknowledged the GOP is experiencing "a cash flow problem" at present. Shah claimed that the GOP has every intention of making full payment to Chevron and noted that the GOP is trying to arrange financing. He further stated that they were not planning to change the overall gas pricing for consumers or lower current fuel, electricity, or food subsidies. Shah claims that President Musharraf is reluctant to increase gas prices at the pump in the midst of current political situation but the GOP hoped to do so "as soon as possible" after elections. Ambassador thanked Shah for his candid evaluation and noted that the Embassy would continue to raise these commercial advocacy issues with appropriate ministries.

Coalition Support Funds

¶7. (C) Ambassador raised concerns about Pakistan's distribution of Coalition Support Funds (CSF). As an example, she noted that the USG had reimbursed USD 55 million to the GOP for helicopter maintenance (Comment: claims paid from July 2006 - February 2007), but this money is not getting to the army for such maintenance. She further

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elaborated that, according to the Pakistani army, these helicopters are now in dire need of depot maintenance and that this issue has the potential to garner a huge amount of negative publicity for our common bilateral objectives. She also commented on the seemingly excessive reimbursement requests such as USD 26 million for barbed wire at the same time the Embassy hears there are no medical supplies for the army troops.

¶8. (C) In response, Shah claimed that the GOP has not received "any paper" for March through November. Shah insisted that Pakistan has submitted over USD 860 million in CSF claims and has not received payment from the USG, aggravating the GOP's cash flow problems since these funds must be paid through other accounts while the GOP waits for reimbursement.

¶9. (C) Shah asked if a new transparent system could be devised to simplify the CSF claims process. He suggested that these payments should be based on "some pre-determined operational indicators such as manpower but minus the overly complex micro details which are currently too cumbersome." Ambassador agreed that we need to devise some sort of new path forward to ensure CSF supports essential projects.

¶10. (C) Shah reiterated that in developing new CSF procedures we should develop (establish) indicators acceptable to both the GOP and USG. Shah requested that the US consider adopting a process similar to what is used for local United Nations or Saudi deployments that would more effectively address the Pakistan military's basic logistical expenses such as rations, supplies, and damage to infrastructure, "which is far better than counting pickets." Ambassador noted that this has become a political problem in the US which requires a solution.

Anti-Money Laundering Legislation (AML)

¶11. (C) Ambassador asked about the status of the AML legislation which has been pending for nearly two years in Parliament. She noted that the USG gave suggestions for improving the language and also commented on the need to set up an independent financial investigative unit in the State Bank of Pakistan. Minister Shah

noted that this unit has been approved by the Ministries and an individual has been earmarked to lead the unit. Shah explained that since the Supreme Court has now approved all actions taken under the Provisional Constitutional Order, the AML will go forward. He further explained that the FIU can become operational with Prime Minister approval because actions taken under the PCO do not require Parliamentary ratification. He noted that the Law Ministry is currently reviewing the constitutionality of this issue. Shah further noted that there will be a meeting of the Executive Committee for AML soon to get the ball rolling.

¶12. (C) Ambassador suggested that Pakistan accept technical assistance from the USG with Department of Treasury experts coming to Pakistan for an exchange visit on establishing a financial monitoring unit. Shah noted that the GOP would welcome such an exchange as soon as possible.

Shared Objectives

¶13. (SBU) Additional Secretary for Finance, Asif Bajwa asked about the status of the USD 200 million shared objectives money and the status of US plans to "projecticize" this aid. Ambassador Patterson noted that the USG priorities are for health and education programs and will be determined on a project by project basis starting with next year's disbursement. Minister Shah requested that the US look to new projects which have not yet been started and noted that the GOP fiscal year will end in June. Shah asked if the US would consider projects in the Pakistan Poverty Alleviation Fund which provides public-private partnership grants for approximately 200 to 300 million rupees (USD 3.3 -5 million) annually. Ambassador reassured Shah that the US is not trying to aggravate Pakistan's current fiscal problems, and that we would review these suggested projects.

¶14. (C) COMMENT: USAID has provided money to the Pakistan Poverty Alleviation Fund in the past, but the majority of these funds have been taken back because of the organization's lack of performance and lack of internal controls.

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¶15. (C) COMMENT CONTINUED. Shah's reference to USD 860 million refers to Pakistan's total CSF claims from March- November 2007. Post had validated USD 282 million out of USD 362 million from Pakistan's March-June 2007 CSF claims. CENTCOM has also validated those claims and OSD is processing them. Payment is expected by mid-February 2008 and should help alleviate some of the GOP cash flow problems. The Office of Defense Representative Pakistan (ODRP) has received Pakistan's July-November 2007 claims totaling USD 506 million. Post can validate USD 342 million which covers expenses for rations, accommodations, medical support, supply, maintenance and transportation. END COMMENT.

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